



IMPLEMENTATION GUIDANCE

DRAFT EFRAG IG 2
Value chain

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EFRAG

sustainability reporting

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This implementation guidance has been developed for use by large listed and unlisted companies that are subject to ESRS. It is therefore not intended for use by non-listed small and medium-sized enterprises (SMEs), which may use the future Voluntary SME standard.

This implementation guidance relates to the sector-agnostic ESRS as adopted by the European Commission on 31 July 2023. Sector-specific standards may add sector specifications to be followed by specific sectors.

How to provide feedback on this document

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About EFRAG

EFRAG's mission is to serve the European public interest in both financial and sustainability reporting by developing and promoting European views in the field of corporate reporting. EFRAG builds on and contributes to the progress in corporate reporting. In its sustainability reporting activities, EFRAG provides technical advice to the European Commission in the form of draft European Sustainability Reporting Standards (ESRS) elaborated under a robust due process and supports the effective implementation of ESRS. EFRAG seeks input from all stakeholders and obtains evidence about specific European circumstances throughout the standard setting process. Its legitimacy is built on excellence, transparency, governance, due process, public accountability and thought leadership. This enables EFRAG to speak convincingly, clearly, and consistently, and be recognised as the European voice in corporate reporting and a contributor to global progress in corporate reporting.



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Table of contents

Summary in 7 key points	4
1. Introduction	5
Structure of the guidance	5
Cross references to the MAIG.....	5
Acronyms used.....	5
2. Navigating value chain under CSRD and ESRS	6
General requirements.....	6
Detailed requirements.....	7
Value chain map	7
2.1 What is the VC?	7
Should IROs linked to all actors in the VC be considered?.....	9
How does leverage or influence over the VC impact reporting?	9
2.2 Why does VC matter?	9
2.3 From own operations to value chain	10
2.4 Which IROs in the VC to disclose?	15
2.5 How do the transitional requirements work?	15
2.6 What is the LSME cap and does it impact my disclosures?	16
3. Frequently asked questions	17
FAQ 1: Where does the VC begin and end?	17
FAQ 2: Are financial assets (loans, equity and debt investments) considered business relationships that trigger VC information?	18
FAQ 3: How should the MA process be organised to properly capture material IROs in the VC?	18
1. Basic principles.....	18
2. Materiality assessment steps	19
FAQ 4: How should information about the VC be disclosed in the context of the materiality assessment?	21
BP-1 - General basis for preparation of the sustainability statement.....	21
SBM-1 - Market position, strategy, business model(s) and VC - 'VC mapping'.....	21
IRO-1 - VC considerations in MA.....	21
IRO-1 - MA methods and assumptions.....	22
SBM-3 - Disclosing the outcome of the MA	22
FAQ 5: Should VC information be included for Policies, Actions or Targets (PATs) Disclosure Requirements?	23
FAQ 6: Should VC information be included for Metrics Disclosure Requirements? ..	24
FAQ 7: How to assess and quantify the impacts of the VC resulting from business relationships?	25
FAQ 8: What is 'reasonable effort' to collect VC data?	26
FAQ 9: How can estimates be developed when primary data cannot be collected from VC counterparties?	28
FAQ 10: Is a case of bribery not involving an employee relevant for the reporting entity?	29
4. VC map	30
VC coverage map of Set 1 ESRS	30
Appendix A: Names of disclosure requirements	32



Summary in 7 key points

NB: this implementation guidance (IG) covers the upstream and downstream value chain (VC) of the undertaking and not its own operations. This guidance should be read together with the MAIG.

1. The undertaking's sustainability statement shall include information about all material impacts, risks and opportunities (IROs) including those that arise or may arise in the context of its business relationships in the upstream and downstream value chain. Business relationships are not limited to direct contractual relationships.
2. The undertaking is not required to include value chain (VC) information in all disclosures, but only when it is connected with material IROs beyond its own operations, due to its business relationships.
3. Therefore, the materiality assessment shall cover the identification of material IROs in the VC, with a focus on where (geographies, activities/sectors, operations, suppliers, customers, other relationships, etc.) in the VC they are likely to materialise. Key disclosures about the undertaking's materiality assessment are SBM-1, SBM-3 and IRO-1 (ESRS 2). They are not limited to but should cover the assessment of IROs in the VC.
4. Topical standards require disclosures about policies, targets and actions (PATs) for material matters. In particular, they require either the disclosure of such PATs or a statement about the absence of them. When describing the PATs for material matters, the disclosure shall include information about how these address material upstream and/or downstream VC IROs.
5. Topical standards require to include VC data only for a few metrics. However, when the undertaking considers that a material IRO in the VC is not sufficiently covered by the requirements in ESRS, it shall include additional entity-specific disclosures, including metrics when such information is necessary in order to enable users to understand the undertaking's material impacts, risks or opportunities.
6. When the undertaking cannot collect primary VC information for the materiality assessment or in order to prepare its disclosures of material IROs after making reasonable efforts, it shall estimate the missing information, using all reasonable and supportable information available without undue cost and effort, including proxies and sector data and other information from indirect sources. The undertaking shall describe in its basis for preparation the metrics using value chain estimation and the resulting level of accuracy.
7. The inclusion of VC information in the sustainability statement does not affect the undertaking's reporting boundary, which correspond to the entities included in the perimeter of its consolidated financial statements. The inclusion of VC information is the extent to which the sustainability statement covers the relationships that all the undertakings in the consolidation perimeter have with their respective VC counterparts, including beyond the first tier. Associates and other investees which are not consolidated in the financial statements are treated as the other business relationships, i.e., as actors in the value chain when this is the case. Also refer to chapter 2.3 below on operational control which is relevant for ESRS E1 *Climate change*.



1. Introduction

8. The objective of this guidance is to support the implementation activities of preparers and others using or analysing ESRS reports, in this case specifically on the value chain information in accordance with the requirements of Articles 19a or 29a of the Directive 2013/34/EU (referred to as the “Accounting Directive”) as amended following the Corporate Sustainability Reporting Directive (referred to as “the CSRD”).
9. The content of this document has been developed on the basis of the July 2023 delegated act.
10. In its implementation support function, EFRAG cannot develop concepts and reporting requirements that go beyond the content of the July 2023 delegated act or interpret Union law. The purpose of the implementation support material is to illustrate how the provisions of the delegated act may be implemented without introducing new provisions. New provisions can only result from future standard setting activities (e.g. future amendments to draft ESRS), if and when applicable in accordance with the EFRAG due process.
11. As an illustration, when the implementation support documents point to a specific approach or methodology that is not detailed in the delegated act, this has to be framed as one of the possible implementation approaches without excluding other possibilities.

Structure of the guidance

12. The document is organised into the following chapters.
 - (a) The next chapter covers how to navigate VC requirements in ESRS which is the basis for the rest of the document.
 - (b) The following chapter covers how an undertaking may implement VC under ESRS by using frequently asked questions with the aim of providing practical guidance.
 - (c) The last chapter includes the ‘upstream and downstream VC map’ that explains the coverage of the upstream and downstream VC as required by ESRS (excluding considerations of entity-specific disclosures and SFDR indicators).

Cross references to the MAIG

13. To avoid duplication and reduce the length of this document, there is significant reference to the Materiality Assessment Implementation Guidance (MAIG) developed by EFRAG. For example, the due diligence aspects related to the materiality assessment (and VC aspects) are covered in that guidance rather than here.
14. Please note that references to the [MAIG are done in this colour](#), whereas references in [green refer to this document](#).

Acronyms used

15. Acronyms used in this document are:
 - (a) CSRD – Corporate Sustainability Reporting Directive;
 - (b) Delegated act – [Commission Delegated Regulation supplementing Directive 2013/34/EU as regards sustainability reporting standards](#);
 - (c) DR – disclosure requirement



- (d) ESRS - European Sustainability Reporting Standards;
- (e) GHG - greenhouse gases or the GHG protocol;
- (f) GRI - Global Reporting Initiative;
- (g) IROs - impacts, risks and opportunities;
- (h) ISSB - International Sustainability Standards Board;
- (i) LSME - ESRS for Listed Small Medium Enterprises (SMEs);
- (j) PAT - policies, actions and targets;
- (k) MA - materiality assessment;
- (l) MAIG - the Materiality Assessment Implementation Guidance; and
- (m) VC - value chain.

Annexes to the delegated act:

[Annex 1](#): ESRS including appendices

[Annex 2](#): Acronyms and glossary of terms

2. Navigating value chain under CSRD and ESRS

- 16. CSRD art 19(a)(3) and 29(a)(3) require that reported information relates to an undertaking's own operations and its upstream and downstream VC, including its products and services, its business relationships and its supply chain.
- 17. ESRS have been developed according to this legal requirement. CSRD does not provide any further definition or guidance about VC. However, with reference to impacts CSRD refers to international instruments of sustainability due diligence which specify how the undertakings are expected to identify, address and report on impacts across their VC.
- 18. The definitions of 'value chain', 'actors in the value chain' as well as 'business relationships' are defined in [Annex 2](#) of the July 2023 delegated act.
- 19. Not all the Disclosure Requirements (DRs) and datapoints in sector agnostic ESRS require the inclusion of information about the undertaking's upstream and downstream VC. In many cases the undertaking is expected to focus on its own operations.

General requirements

- 20. The general requirements relating to all disclosures on VC can be found in ESRS 1 *General requirements*:
 - (a) The general requirements for reporting on the VC are in chapter 5;
 - (b) Application Requirements AR 17 set out guidance on 'Estimation using sector averages and proxies'; and
 - (c) Lastly, but importantly, ESRS 1 contains specific transitional provisions with respect to VC in chapter 10.2.
 - (d) ESRS 1 requires the inclusion of material VC information when this is necessary to allow users to understand the undertaking's material IROs and to produce information that meets the qualitative characteristics of information set for in Appendix C of ESRS 1 (ESRS 1 paragraph 65). This is a principles-based approach that works on top of the specific datapoints in ESRS that require to include specific VC information. This means that where necessary (i.e. reflecting the outcome of the materiality assessment), the undertaking shall cover VC.



Detailed requirements

21. Other detailed requirements about value chain can be found in ESRS as follows:

- (a) ESRS requires disclosures concerning the process and outcomes of the materiality assessment are covered in ESRS 2 *General disclosures* (IRO-1 and SBM-3), accompanied by SBM-1. See below in [FAQ 4 How should information about the VC be disclosed](#) in the context of the MA as well as rows 1 to 3 of the VC coverage map of Set 1 ESRS. For details about the materiality assessment process, please refer to the [MAIG](#) and for the related VC aspects please see [FAQ 3 How should the MA process be organised to properly capture material IROs in the VC](#) below. Please also refer to [MAIG FAQ 10 Should the assessment of IROs rely on quantitative information?](#)
- (b) All the topical standards require undertakings to disclose their policies, actions and targets for material IROs; to the extent that such policies, actions and targets address material IROs in the VC, this will be reflected in the disclosures. The minimum disclosure requirements with respect to policies, actions and targets require information on scope such as whether it relates to the VC per ESRS 2 paragraphs 65(b), 68(b), 80(c). (see [FAQ 5 Should VC information be included in PAT disclosures?](#)). Within the disclosures about policies, actions and targets, the Social topical standards ESRS S2 *Workers in the value chain*, ESRS S3 *Affected communities* and ESRS S4 *Consumers and end-users* provide a framework for reporting on material IROs related to these groups of people in the VC and their management. As a reminder, the undertaking can comply by disclosing that it has not adopted policies, actions and targets with reference to the relevant material sustainability matter and provide reasons for this. It may also report a timeframe in which it aims to adopt them (ESRS 2 paragraphs 62 and 72). Please refer to rows 4 and 5 of the VC coverage map of Set 1 ESRS.
- (c) There are only few sector-agnostic metrics in topical ESRS that require VC information (see [FAQ 6 Should VC information be included in metric DRs?](#)). ESRS S2 to S4 for instance do not include metrics per se. The other metrics do not refer to the value chain. However, this includes some information about procured materials, please refer to rows 6 to 8 of the VC coverage map of Set 1 ESRS.
- (d) Finally, when an undertaking concludes that a material IRO is not sufficiently covered by an ESRS, it shall provide additional disclosures to enable users to understand its IROs. (ESRS 1 paragraph 11 and AR 1 to 5). This may include information, including when appropriate metrics, about a material IRO in the VC.

Alignment with ISSB and GRI

The definitions of value chain under ISSB and GRI frameworks are aligned with ESRS.

Value chain map

22. Chapter 4 of this document presents the VC map which illustrates the type of coverage of VC information that is required by each specific Disclosure Requirement in sector agnostic ESRS. This also includes which metrics require inclusion of VC data in the actual calculation.

2.1 What is the VC?

23. While the focus of this Implementation Guidance is on upstream and downstream VC, the definition of Value chain in [Annex 2](#) of the delegated act is broader than the upstream and downstream VC, as it also includes own operations. VC is defined as *the*



What is the difference between value chain and supply chain?

In short, the VC includes the supply chain. The supply chain is the actors in the VC upstream from the reporting entity. However, VC also includes downstream entities along with the supply chain.

The supply chain provides products including raw material or components or services that are used in the development of the undertaking's products or services. Depending on the position in the VC, an undertaking's supply chain can be part of the downstream VC of another undertaking.

In some industries, upstream or downstream refers to specific points in the chain rather than with reference to the reporting undertaking's position in the chain.

However, there are other entities and individuals that are connected to the undertaking's operations, products and services without being "suppliers", e.g., local police protecting the undertaking's assets, as they may cause an impact by e.g., using excessive force on people trespassing. In this case, there is no business relationship, but there is a value chain impact. It may meet the materiality threshold if it is considered severe enough.

full range of activities, resources and relationships related to the undertaking's business model and the external environment in which it operates. A value chain encompasses the activities, resources and relationships the undertaking uses and relies on to create its products or services from conception to delivery, consumption and end-of- life. Relevant activities, resources and relationships include:

- (a) those in the undertaking's own operations, such as human resources;*
- (b) those along its supply, marketing and distribution channels, such as materials and service sourcing and product and service sale and delivery; and*
- (c) the financing, geographical, geopolitical and regulatory environments in which the undertaking operates.*

Value chain includes actors upstream and downstream from the undertaking. Actors upstream from the undertaking (e.g., suppliers provide products or services that are used in the development of the undertaking's products or services). Entities downstream from the undertaking (e.g., distributors, customers) receive products or services from the undertaking.

24. ESRS use the term "value chain" in the singular, although it is recognised that undertakings may have multiple value chains.

25. According to this definition, the VC issues addressed in this implementation guidance include both upstream and downstream actors and their activities. Actors or undertakings upstream from the reporting undertaking (e.g.,

suppliers) provide products or services that are used in the development of the undertaking's own products or services. Actors downstream from the reporting undertaking (e.g., distributors, customers, waste management) receive, use products or services of the reporting undertaking or waste stream by the customers or end-users.

26. [Annex 2](#) defines business relationships as *'[t]he relationships the undertaking has with business partners, entities in its value chain, and any other non-State or State entity directly linked to its business operations, products or services. Business relationships are not limited to direct contractual relationships. They include indirect business relationships in the undertaking's value chain beyond the first tier, and shareholding positions in joint ventures or investments.'*

27. Setting out the VC activities may help identifying the VC actors.



Should IROs linked to all actors in the VC be considered?

28. ESRS does not require information on each and every actor in the VC, but rather the inclusion of material VC information, i.e., when material IROs arise in the VC (ESRS 1 paragraph 64). When assessing material IROs, all relevant actors (both from direct and indirect relationships) are to be considered. However, the assessment should focus on relationships that are likely to be associated with material IROs, for example relationships with:
- (a) those actors that are associated with 'hot spots' that expose to the likelihood of actual and potential impacts (therefore generating impacts on people and/or environment, which can in turn be sources of risks and opportunities); or
 - (b) those actors with respect to which the business model of the undertaking shows key dependencies in terms of products or services (therefore generating risks and opportunities for the undertaking).

How does leverage or influence over the VC impact reporting?

29. In some cases, an undertaking may have leverage or be able to exert influence over actors in its VC. Examples include where the undertaking is a large supplier or customer and so exert influence on the business relationships to manage its impacts.
30. In other cases, its ability to obtain the necessary VC information as well as its capacity to contribute to or influence the management of IROs arising in the VC, may be limited given the nature or the absence of direct contractual arrangements, the level of control that it exercises on the operations outside the consolidation scope and its buying power.
31. However, leverage does not affect whether IROs that arise in the VC are material or not. Leverage may affect the ability of the company to obtain data from its counterparties in the VC. This may be relevant for the reporting of material impacts as well as for reporting metrics including entity-specific information (See ESRS 1 AR 1 to AR 5) and may lead the undertaking to use estimates and proxies.

2.2 Why does VC matter?

32. CSRD and ESRS require that the sustainability statement include information about the upstream and downstream VC.
33. The reason for this is that the major impacts, or major risks and opportunities deriving from impacts or dependencies, of a reporting undertaking often occur in its upstream or downstream VC rather than in its own operations. Therefore, focusing on own operations would provide only a partial picture of the impacts on people and the environment connected to the undertaking's activities, products and services. Furthermore, this would not allow for an appropriate identification of risks and opportunities.
- (a) For example, consider an EU garment and apparel company that sells basic T-shirts produced in a country outside the EU by an external supplier and that reports under ESRS. The company may pay its employees an adequate wage under collective bargaining agreements for its operations in the EU. However, assuming the external supplier is based in a country outside the EU where the remuneration paid to the supplier's employees is below the adequate wage benchmark for the country and freedom of association in that country may not be allowed, the reporting undertaking would not provide a relevant depiction of its impacts if it was to consider



- only its own employees when determining the scope of its actual and potential material negative impacts. In other terms, material impacts on working conditions may be identified within the workforce in its upstream VC (for this particular supplier).
- (b) Another example is a European retailer with wooden toys made in a factory outside the EU, where legal requirements are less stringent. The toy-making process has several environmental and health and safety risks, due to dust and chemicals. There is therefore a significant risk that the workers and the local communities are exposed to severe occupational hazard exposures and health risks – important when considering impact materiality. From a financial materiality perspective, if the officials in that location start upholding laws rather than accepting bribes as is currently the case, it could result in significant fines or even possible closure for the manufacturer. This could have a direct and significant financial impact on the European retailer.
 - (c) Similarly, Scope 3 GHG emissions are expected to be material for many or most undertakings¹.

2.3 From own operations to value chain

The reporting group as starting point

- 34. ESRS 1 paragraph 62 states: “The sustainability statement shall be for the same reporting undertaking as the financial statements.” In the [Accounting Directive](#), a group is defined as “a parent undertaking and all its subsidiary undertakings”.
- 35. For sustainability reporting, groups must include information about material IROs of the subsidiaries. The elimination of internal transactions following the financial accounting consolidation procedures for the preparation of the financial statements does not apply in sustainability reporting. The underlying impact that occurs in the group’s operations are in scope of the reporting, when material, as well as the ones identified in the VC.
- 36. Sometimes subsidiaries are excluded from the financial reporting consolidation on the basis of materiality, for practical reasons. Please refer to the [MAIG chapter 5.2 FAQs on financial materiality](#) for considerations of these for the sustainability statement.
- 37. The information about material IROs of the parent and subsidiaries (including leased assets under IFRS) is ‘extended’ to cover VC information. This is defined in ESRS 1 paragraph 63 as information on the material IROs connected with the undertaking through its direct and indirect business relationships in the upstream and/or downstream value chain.
- 38. Associates and joint ventures may also be actors in the value chain of the reporting undertaking, such as when they are customers or suppliers. When this happens, the impacts arising from this business relationship are treated as impacts connected to any business relationship of the same nature (i.e. as impacts connected with customers or suppliers), irrespective of the accounting treatment in the financial statements. When they are not actors in the value chain, the reporting shall consider the investment relationship as potential source of material impacts, risks and opportunities.

¹ https://cdn.cdp.net/cdp-production/cms/guidance_docs/pdfs/000/003/504/original/CDP-technical-note-scope-3-relevance-by-sector.pdf

39. For environmental matters, ESRS refer to the concept of *operational control* to identify situations where information about IROs of a site, an asset or an entity outside the financial control perimeter have to be reported.

Operational control – E standards

40. ESRS E1 paragraph 46 specifies how to apply this approach for GHG emissions. It requires including in the reported GHG emissions, the data of the joint ventures, associates, unconsolidated subsidiaries (investment entities) and contractual arrangements that are joint arrangements not structured through an entity (i.e., jointly controlled operations and assets), to the extent of the operational control of the undertaking over them.
41. ESRS E1 AR 40 clarifies the definition in Annex II that the undertaking shall include 100% of the GHG emissions of the entities it operationally controls. It provides an example of where an undertaking has a contractually defined part-time operational control, it shall consolidate 100% the GHG emitted during the time of its operational control.
42. This means that the GHG emissions reported will reflect the terms and conditions of the relevant agreements. For example, an undertaking (A) with a joint venture under joint control with a third party (C), with A as the operator of the activities in a certain phase of the production process and C is the operator in another phase of that process. A would report in its scope 1 and 2 the GHG emissions that pertain to the phase that it operationally controls.
43. Whether referring to associates, joint arrangements and unconsolidated subsidiaries under operational control, ESRS E1 requires disclosing the Scope 1 and 2 emissions of these undertakings separately from the ones related to the consolidated group for financial reporting (paragraph 50(b)).
44. ESRS E2-4 *Pollution of air, water and soil* also specifically includes those emissions from facilities under the operational control of the undertaking. Similarly, ESRS 4 *Biodiversity and ecosystems* in paragraph 16 also includes sites under the operational control of the undertaking.

Operational control (over an asset, a site or a plant, JVs, Associates etc.)

Defined by Annex II of the July 2023 delegated act **as the situation where the undertaking has the ability to direct the operational activities and relationships of the entity, site, operation or asset.**

AR 40 of ESRS E1 also explains, in the context of GHG emissions, that this may happen “when the undertaking holds the license - or permit - to operate the assets from these associates, joint ventures, unconsolidated subsidiaries (investment entities) and contractual arrangements”.

A company has operational control over an entity, site, operation or asset if it has the ability to direct their operational activities and relationships. This occurs independently if it is the parent or one of its subsidiaries (i.e. it refers to the consolidated group). This is the case where, for example, the company has the full authority to introduce and implement the operating policies, which often implies also executing such operations; or when it is legally recognized - with implied legal rights and obligations - under certain regulations (for example the EU Emissions Trading system) as an "operator" of a facility.

Having operational control does not mean that an undertaking necessarily has authority to make all decisions concerning an operation. For example, big capital investments will likely require the approval of all the partners that have joint control (per IFRS 11).

Sometimes a company can have joint control over an operation, but not operational control. This would require analysis of the contractual arrangements to determine whether any one of the partners has the authority to introduce and implement its operating policies.



45. Beyond these three standards, there may be circumstances where the concept should be applied such as where bodies of water have been impacted due to pollution by assets, sites or entities under operational control.
46. ESRS 2 BP 2 requires that the undertaking describes its basis of preparation including indicating whether operational control was considered or not (see paragraph 152).

Operational control – S standards

47. Undertakings should separately consider any workers related to assets, sites or operations under operational control to determine whether such workers meet the definition of own workforce and workers in the value chain. Please refer to ESRS S1 *Own workforce* and S2 *Workers in the value chain* as relevant. Operational control is not relevant for ESRS S3 and S4 respectively.

Associates and joint arrangements

48. The starting point for ESRS reporting is not equity accounting or proportional consolidation as one finds under financial reporting. ESRS 1 paragraph 67 states that when associates or joint ventures are part of the undertaking's VC, for example as suppliers or customers, the undertaking shall include information required by ESRS 1 paragraph 63 consistent with approach adopted for the other business relationships in the VC. Furthermore, when determining impact metrics, the data in relation to the associates or joint ventures are not limited to the share of equity held but shall be considered on the basis of the impacts that are directly linked to the undertaking's products and services through its business relationships (ESRS 1 paragraph 67). To illustrate this, an undertaking, P, produces chairs with wood sourced from another undertaking that is classified as an associate (A) for financial reporting. P holds an equity share in A of 30%. P buys 10 tons of wood from A to produce its chairs. P will treat A in the same way as any other supplier when considering the impacts connected with the wood purchased from A. Therefore, in this case, the impacts related to the 10 tons of wood purchased rather than estimating its impacts by using its equity share in A.
49. Where associates and joint arrangements do not form part of the value chain as suppliers or customers, they are treated as investments. Investments form part of the undertaking's business relationships (as defined). As such, they may give rise to impacts that are connected with the undertaking and that are to be considered in the materiality assessment and reported when material. However, topical ESRS do not have specific reporting requirements that indicate how to measure these impacts, apart from GHG Scope 3 Category 15 disclosures where significant in accordance with ESRS E1 paragraph 44(c), AR 39(a) as explained in AR 46 and AR 48.

Other investments, no further transactions.

50. Business relationships with the investees may give rise to impacts that are connected with the undertaking and that are to be considered in the materiality assessment and reported when material. There are no specific requirements in topical standards on how to measure impacts that are connected with the undertaking through its investments without joint control and/or significant influence, so generally below 20%, apart from GHG Scope 3 Category 15 disclosures as explained in paragraph 49.

Entity-specific disclosures

51. As explained in paragraph 54(b) below, in the cases above, apart from the materiality assessment process, the undertaking may also have to provide entity-specific information including on the VC in terms of ESRS 1 paragraph 11.



Mapping of financial reporting concepts to sustainability reporting

52. The following table illustrates the treatment of impacts arising from investments of the undertaking depending on their accounting treatment in the financial statements:

	Common characteristic(s) ²	Accounting treatment	Measuring impacts by metrics in topical standards
Subsidiary	Control or 50%+1 of voting rights or de facto control less than 50% of voting rights	Include 100% of assets, liabilities, income and expenses	Fully included (scope of consolidation is the same as financial reporting)
Associate	Significant influence, usually between 20% and 50% of voting rights; ability to influence the decision making through the appointment of a director to the board.	Investor recognises its share of profits and losses and add to value of investment in associate on balance sheet in a single line item (no proportional consolidation line by line)	Operational control ³ : GHG emissions to the extent of operational control. (ESRS 1 par. 67) Associates that are actors in the value chain - based on impacts connected with the undertaking's products and services through transactions. Associates with other business relationships (i.e. investees only) There are no specific indications for metrics in the sector agnostic standards on how to measure impacts connected with the undertaking through its associates, where they are not actors in the value chain (except for category 15 of GHG protocol).
Investments Trading	Less than 20% held for short term gain	Recognised at fair value; dividends in profit or loss.	There are no specific indications in metrics of the topical standards on how to measure impacts connected with the undertaking through its investments (except for category 15 of GHG protocol in ESRS 1).
"Strategic"	Less than 20% not held for short term gain		
Joint venture	Joint control with rights to net assets of the arrangement. Always a separate entity.	Same as for associates	Same as for associates except for joint operations where the assets/liabilities belong to the reporting undertaking and so form part of own operations.
Joint operation	Joint control with rights to assets, obligations for the liabilities relating to the arrangement. Not necessarily a separate entity.	Recognises its assets, liabilities, revenue, expenses including any share from items held jointly (proportional consolidation).	

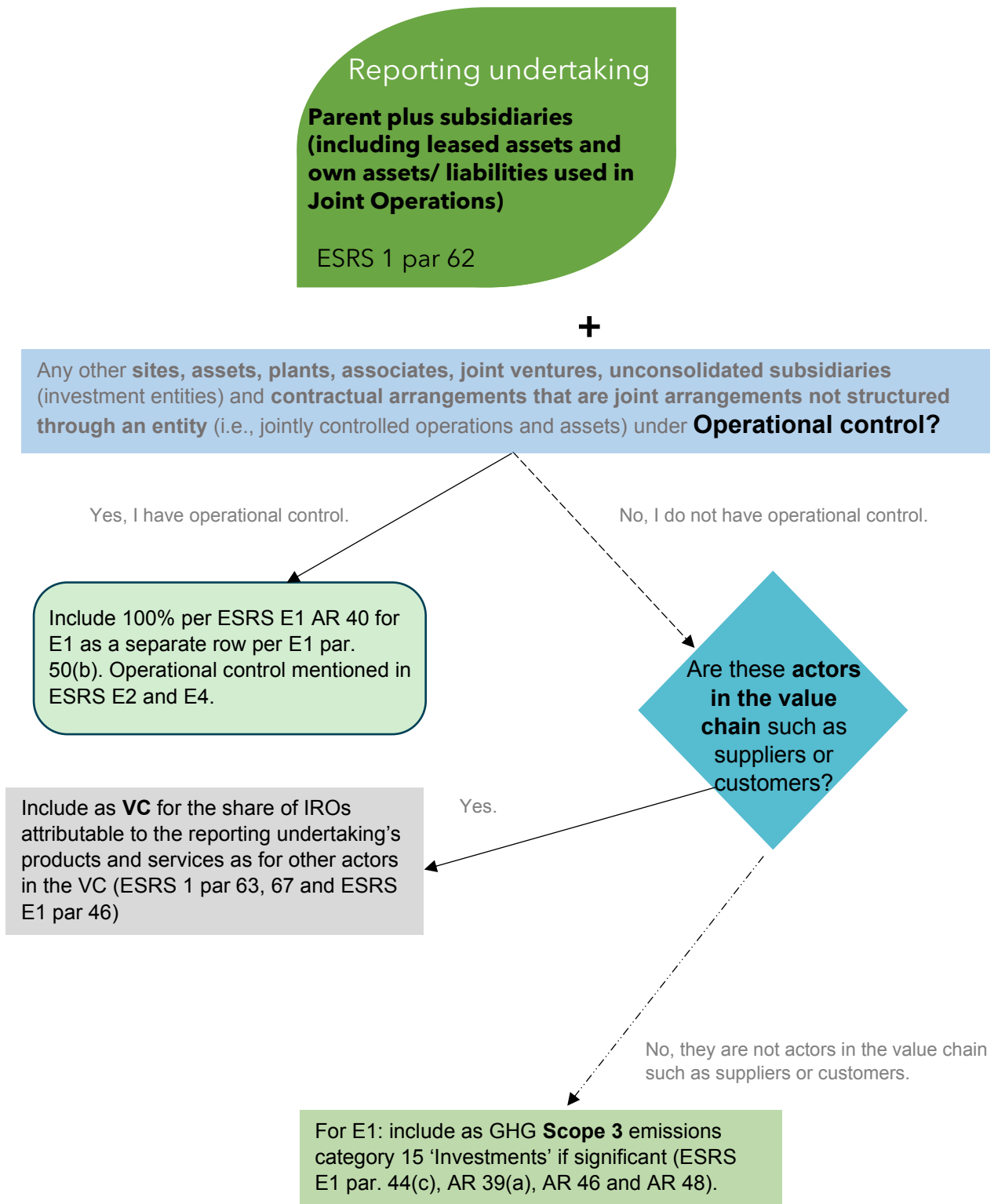
² Please note that this is a very simplified description of the financial reporting requirements (and may differ between IFRS and local GAAP used in European countries) and so does not capture the nuances involved in classifying investments.

³ Operational control can also apply to assets under joint control proportionally consolidated. The related GHG emissions then reflects the terms and conditions of the arrangement.



Reporting boundary decision tree

53. The following decision tree summarises some of the important aspects related to the E-standard above:



2.4 Which IROs in the VC to disclose?

54. The two overarching requirements in ESRS 1 that are applicable are:
- (a) paragraph 63 requiring information on material IROs connected with the undertaking's upstream and downstream VC; and
 - (b) paragraph 11 requiring entity-specific information when a reporting undertaking concludes that a material IRO is not covered sufficiently by an ESRS, to enable users to understand such IRO. Such entity-specific information is expected to cover both IROs in own operations and IROs in the upstream and downstream VC, when they are material.
55. An impact may be material to the reporting undertaking if it arises in any part of the VC, including at any tier of its upstream VC or supply chain. In this regard, in the IRO assessment in the VC, the undertaking has to consider IROs that it may be connected to through its operations, products or services by business relationships. (Also see [MAIG FAQ 2 What is meant by the undertaking being "connected" with an impact?](#)).
56. The identification of IRO in upstream and downstream VC is embedded in the materiality assessment (ESRS 1, Chapter 3 - Double materiality as the basis for sustainability disclosure). For further information about materiality, please consult the [MAIG](#).

2.5 How do the transitional requirements work?

57. The general transitional provisions in ESRS 1 [paragraph 130](#) onwards allow a temporary limit to the information on the VC to be reported during the first three years of reporting under ESRS. Specifically, preparers are required to consider VC in their materiality assessment, but the data gathering aspects are limited in their first three years of reporting.
58. The transitional provisions are intended to provide reporting undertakings with more time to prepare for the new reporting regime in case not all the necessary information regarding VC is available. The transitional requirements are optional, i.e., the undertaking can decide whether it wants to use them or not and they apply whether the VC actor is an SME or not.
59. The steps an undertaking can consider during this time may include:
- (a) Stakeholder engagement and other enhancements to the materiality assessment;
 - (b) Preparation of technological and other infrastructure required for the reporting;
 - (c) Updating of contracts with actors in the VC to reflect status of new implemented policies or target tracking, such as foreseeing the provision of periodic information; and
 - (d) Improved knowledge about the structure of the VC, specific actors involved and associated impacts and dependencies.
60. The transitional requirements (ESRS 1 paragraph 132) foresee that if not all the necessary VC information is available during the first three years of the reporting undertaking's sustainability reporting under ESRS, the undertaking shall explain:
- (a) The efforts made to obtain the necessary information;
 - (b) The reason why it could not obtain the necessary information; and



- (c) Its plans to obtain the necessary information in the future.
61. In addition, during the transitional period, reporting undertakings may limit information to in-house data (such as data available to the undertaking and publicly available information) to disclose information on policies, actions and targets for the VC (ESRS 1 paragraph 133 (a)).
62. In addition, with reference to metrics, the undertaking is not required to include upstream and downstream VC information, except for datapoints derived from other EU legislation, as listed in ESRS 2 Appendix B (see ESRS 1 paragraph 133 b)) during the transitional period.
63. Starting from its fourth year of reporting under ESRS, the undertaking shall include VC information according to ESRS 1 paragraph 63 (ESRS 1 paragraph 135) and as explained in this document.
64. In addition to the transitional provisions described above, Appendix C of ESRS 1 specifies that for ESRS E1-6 *Gross Scopes 1, 2, 3 and Total GHG emissions*, undertakings or groups with less than average of 750 employees at balance sheet dates, may omit datapoints on Scope 3 emissions and total GHG emissions for the first year of preparation of their sustainability statement. Similarly, the disclosure requirements for ESRS S2 *Workers in the value chain*; ESRS S3 *Affected communities* and ESRS S4 *Consumers and end-users* may be omitted for the first two years by undertakings who have 750 or less employees during the financial year.

Transitional provision with respect to entity-specific disclosures

65. While not exclusively related to the VC, given that entity-specific disclosures may trigger the inclusion of VC information, the transitional provision applying to entity-specific disclosures (ESRS 1 paragraph 131) is also relevant here.
66. In the first three annual sustainability statements, when the reporting undertaking is defining its entity-specific disclosures, it may as a priority:
- (a) Include disclosures it previously reported (where these meet the qualitative characteristics of information per chapter 2 of ESRS 1); and
 - (b) Add disclosures to cover those material sustainability matters in its sector(s) using available best practice and/or available frameworks (such as IFRS or GRI sector-specific requirements).

2.6 What is the LSME cap and does it impact my disclosures?

67. Article 29b(4) of the CSRD limits the VC information that the ESRS shall require undertakings in scope of the CSRD to obtain from small-medium enterprises (SMEs) for their reporting under ESRS. ESRS may not require disclosures which will result in reporting undertakings having to request information from the SMEs in their VC if such information goes beyond the disclosures required in the listed SME (LSME) ESRS.
68. This limitation is often referred to as the 'LSME cap' and it aims at limiting the burden for SMEs and embed proportionality in the ESRS.
69. The LSME ESRS is still under development. EFRAG expects to be able to consult on LSME Exposure Draft toward the end of 2023 and one of the aspects to cover in the consultation is the approach to the implementation of the LSME cap.



3. Frequently asked questions

70. This chapter provides further practical guidance on the VC principles described in the previous chapter.

FAQ 1: Where does the VC begin and end?

71. ESRS requires the undertaking to identify and assess material IROs across its entire VC from a double materiality perspective. In this regard:

- (a) relevant impacts are defined as those that are connected with the undertaking, which includes when they are either caused by or contributed to or that are directly linked to the undertaking's operations, products or services through a business relationship. The relevant impacts are not ringfenced by proximity or contractual relationship, but by the fact that they occur in connection with the processes at any stage of the VC that contribute to the undertaking's operations, products or services, or that result from the use or end-use of those products or services. Conversely, the impacts of actors in the value chain not connected to the undertaking's operations, products and services are outside of the scope of impact materiality (Also see [MAIG FAQ 2 What is meant by the undertaking being "connected" with an impact?](#)); and
- (b) relevant risks and opportunities are those attributable to business relationships, in particular with actors in the VC that are beyond the scope of consolidation used for the preparation of financial statements for financial materiality (ESRS 1 par. 49).

72. To assess potential and actual impacts, it is important that the undertaking identifies in particular:

- (a) the location and characteristics of suppliers including beyond the first tier of their upstream VC or supply chain;
- (b) the users of their services and goods;
- (c) how the goods are treated in terms of waste at the end of their life; and
- (d) who may be affected by their services and goods.

73. See [FAQ 7 How to assess and quantify the impacts of the VC resulting from business relationships?](#) below for recommendations on how to organise the processes to identify and assess material impacts across the VC.

74. To assess risks and opportunities, the undertaking considers its own dependencies on natural, human and social resources. The undertaking identifies potential changes in the availability, price and quality of such resources, which are sources of risks and opportunities, including those stemming from its upstream and downstream VC. The following three examples illustrate this concept:

- (a) A company has a tier-1 supplier, that provides it with the main components of its final products, in a region with water scarcity. To provide the components, the supplier needs minerals from a mining company which is heavily dependent on a supply of water. As such, this supplier would be at risk if one of the mines was no longer able to access sufficient water from its existing sources. Consequently, the supplier may face physical risks in the future due to the water scarcity in the region, which could lead to operational disruptions and increased costs. This situation could lead to discontinuities in the supply of steel with disruptions in production.



- (b) If the buying price does not cover the cost of a product bought, it may increase the pressure on the working conditions at suppliers. If the purchasing department of the reporting entity does not understand lead times or ignore lead times when ordering this could have a negative effect on the workforce of their contractual partners in terms of overtime, accidents or use of forced labour.
- (c) A company active in the food sector needs to be constantly supplied with natural key inputs (such as flours). One of its main suppliers is active in a region at high risk of biodiversity loss and following the request by local authorities to restore damaged habitats it has a more variable production of key natural inputs and higher production costs. This situation could lead to disruptions in the supply of key natural inputs with consequences in the production of the company active in the food sector. Active spot markets with delivery close to the company may alleviate the risk of disruption but may have implications for pricing.

FAQ 2: Are financial assets (loans, equity and debt investments) considered business relationships that trigger VC information?

- 75. Yes. Business relationships and VC as defined in Annex II of the July 2023 delegated act does not exclude any types of activities and business relationships.
- 76. ESRS 1 AR 12(b) illustrates that where the reporting undertaking provides financial loans to another enterprise that ultimately results in the contamination of water and land surrounding the operations of such enterprise, this negative impact is connected with the reporting undertaking by way of the relationship created by the loan agreement.
- 77. Per paragraph 49, for equity investments there is currently only disclosures under Category 15 of GHG emissions where significant under ESRS E1.
- 78. EFRAG plans to work on the development of further draft standards or guidelines for Financial Institutions and on that occasion, specific solutions will be consulted on for comments.

FAQ 3: How should the MA process be organised to properly capture material IROs in the VC?

1. Basic principles

- 79. The materiality process is the process by which the undertaking determines material information on sustainability impacts, risks and opportunities and this includes information related to the VC, but not information on each and every actor in the VC. Therefore, for the identification of impacts, risks and opportunities within the materiality assessment, the undertaking should focus on the parts of their value chains where material impacts are most likely to occur. As outlined in the [MAIG, chapter 3 How is the materiality assessment performed?](#), the undertaking should design a process that is fit for purpose as required by ESRS 1 chapter 3 and disclose per the requirements set out in ESRS 2 IRO-1. An undertaking, based on its specific facts and circumstances, shall design a process that is fit for purpose, including consideration of the depth of the assessment. This principle also applies to the value chain.
- 80. The ESRS clarify that the materiality assessment process is informed by the due diligence process.



2. Materiality assessment steps

81. The guidance on the organisation of the materiality assessment process can be found in the [MAIG, chapter 3 How is the materiality assessment performed?](#) As explained there (emphasis added): *ESRS do not mandate how the materiality assessment shall be conducted by an undertaking, or how the process should be designed. No one process would suit all types of economic activities, location(s), **business relationships** or value chains (upstream and/or downstream) of all the undertakings applying ESRS. An undertaking, based on its specific facts and circumstances shall design a process that is fit for purpose considering the requirements of ESRS 1 Chapter 3, and what needs to be disclosed regarding the materiality assessment and its outcome (see ESRS 2 IRO-1, IRO-2 and SBM-3). Therefore, the ESRS provide several aspects that an undertaking takes account of when designing the materiality assessment process.*
82. With this caveat, the [MAIG](#) provides guidance for the general organisation of the MA process. The guidance below reflects how VC aspects can be considered in the possible process.

Step A. Understand the context

83. As explained in the [MAIG](#), the first step in the MA process is about understanding the context in which the undertaking operates. Therefore, the undertaking needs to understand its VC in terms of business actors involved, their size, the sectors or nature of their activities, geographical locations, and processes. This is a starting point for the identification of where IROs are likely to arise.
84. The context also includes understanding the undertaking's strategy and business model and how they are connected to possible material IROs.
85. The strategy of the undertaking will influence its business model which will focus on its own operations but also include aspects around its up- and downstream value chain. All of this will be considered its materiality assessment.
86. The undertaking can consider tracing or mapping its VC activities and actors to identify whether and which parts of its value chains are in areas of heightened risks. In some cases, if the undertaking does not have reliable information on the geographical location of its VC (for example beyond the first tier), it may map the IROs associated with global value chains for materials, products and services it uses or produces, to the extent that they are relevant for its VC. For example, a chair manufacturer may use products such as steel, wood, foam and fabric in its business. These raise questions around origin of components (oil used to produce foam and cotton for the fabric) and the transport to the undertaking. Are there any environmental (deforestation, biodiversity, water usage) or social issues (working conditions, impact on communities) in countries of origin of the components? What are the sustainability matters pertaining to the consumers? Here the sales channels may be relevant as well as the ability to re-use, re-cycle or up-cycle the furniture at the end of its life.
87. As explained in the general instructions in the [MAIG](#), engagement with affected stakeholders can support the assessment and validation of the impacts the undertaking should also identify [likely] affected stakeholders and consider engaging with them. See also [MAIG FAQ 17 What is the role of silent stakeholders and how to consider them?](#)



Step B. and Step C: Identification of actual and potential IROs as well as Assessment and determination of the material IROs

88. Identification and assessment of impacts can be challenging for those parts of the VC where the undertaking is not able to trace the materials and products. ESRS 2 paragraph 5 c) requires a description of the extent to which the disclosures cover the undertaking's upstream and downstream VC.
89. The undertaking should aim to gather reliable data from actors in its VC. If this is not possible after having made reasonable efforts, it may rely as appropriate on sources of secondary data. Secondary data include information such as publicly available reports and studies, sector proxies, data from local, regional or national authorities, newspaper articles, databases, etc. to estimate the IROs where this provides relevant and faithfully representative information.

Assessment of the involvement of the undertaking with the VC

90. The undertaking is required to provide a description of whether the material impacts, risks and opportunities connected to the undertaking as well as those that are directly linked to its operations and services in its upstream or downstream value chain (ESRS 2 SBM-3 paragraph 48 (a)).
91. As explained in [MAIG, FAQ 2 What is meant by the undertaking being 'connected' with an impact?](#) the undertaking may for instance be involved in a breach of labour standards through its procurement and payment policies and practices, or even by sourcing from suppliers with cases of labour rights abuse.
92. The contribution to the impacts in the VC may concern direct business relationships. However, the undertaking may find itself contributing to impacts that occur in more distant parts of the VC. This may for instance be the case when the undertaking or its direct suppliers are using commodities or components whose production is associated with severe systemic impacts, such as palm oil or coltan. Similarly, the undertaking may be contributing to impacts that are a result of the use of its products such as oil and gas derived fossil fuels, plastics contributing to microplastics pollution, cigarettes, or pesticides.
93. An undertaking can cause, contribute or be directly linked to an impact in the value chain. Distinguishing the type of involvement is important given that it could lead to a different assessment or categorisation of the negative impact.

Environmental topical standards on materiality assessment

94. Environmental standards use the concept of life cycle or life cycle assessment, which also covers value chain, in the context of materiality assessment. In particular:
 - (a) ESRS E2 AR 18: "In order to assess materiality, the undertaking may consider Commission Recommendation (EU) 2021/2279 on the use of the Environmental Footprint methods to measure and communicate the life cycle environmental performance of products and organisations."
 - (b) ESRS E3 AR 14: "The undertaking may rely on primary, secondary or modelled data collection or other relevant approaches to assess material impacts, dependencies, risks and opportunities, including Commission Recommendation 2021/2279 on the use of the Environmental Footprint methods to measure and communicate the life cycle environmental performance of products and organisations (Annex I - Product Environmental Footprint; Annex III - Organisation Environmental Footprint)."



- (c) ESRS E5: the concept of 'life cycle' is so important that is part of the objective in paragraph 3 and AR 6 explains its use to assess IROs in own operations and the VC.

FAQ 4: How should information about the VC be disclosed in the context of the materiality assessment?

95. The disclosure of information about the VC is required in two steps, as a component of (i) the materiality assessment process and of (ii) the outcome the materiality assessment.

BP-1 – General basis for preparation of the sustainability statement

96. ESRS 2 paragraph 5(c) requires disclosing to which the extent the sustainability statement covers the undertaking's upstream and downstream VC. Therefore, in addition to metrics, this applies to all the steps below, to the extent that material IROs arise in the upstream and downstream VC.

SBM-1 – Market position, strategy, business model(s) and VC – 'VC mapping'.

97. To provide an understanding of where in the undertaking's VC material IROs may arise, ESRS 2 paragraph 42(c) in SBM-1 requires the following description of its VC:
- (a) the main features of its upstream and downstream VC;
 - (b) the undertaking's position in its VC;
 - (c) description of the main business actors and their relationship to the undertaking:
 - (i) key suppliers,
 - (ii) key distribution channels,
 - (iii) key customers and/or end-users.
98. Identifying the key actors requires judgement, to reflect the specific circumstances of the undertaking's VC and should consider both impact and financial materiality criteria.
99. The mapping of the VC for material impacts is expected to use the sustainability due diligence process, when it is in place. However, the due diligence process may go beyond such mapping per se as explained below, looking at the impacts throughout the VC and identifying potential 'hot spots' by cross-referencing countries where materials are produced to social and environmental risk databases (i.e., Type of impact by Country by Actor in the VC). These hotspots may then be further investigated.

IRO-1 – VC considerations in MA

100. Subsequently, the undertaking shall describe its materiality assessment process, including in relation to the VC, and the extent to which it may be informed by the due diligence process.
101. ESRS 2 IRO-1 paragraph 53 (b) (ii) requires an overview of the process to identify, assess and prioritise the undertaking's impacts it is involved through its own operations or because of its business relationships. Similarly, paragraph 53 requires disclosing an overview of the process used to identify, assess, prioritise and monitor risks and opportunities that have or may have financial effects, which may arise due to its business relationship in the VC. In fact, the business relationships in the upstream and



downstream VC shall be considered also in the context of assessing the materiality of risks and opportunities and not just for impacts (ESRS 1 paragraph 66).

102. The disclosure that meets these requirements could be structured as follows:
- (a) the types of VC relationships that were considered in the materiality assessment;
 - (b) the methods the undertaking used, and
 - (c) the sustainability topics that were evaluated.
103. For impacts, based on the initial mapping, the undertaking may focus on areas where actual or potential impacts could arise, which in turn reflects areas where the negative impacts are or could be severe. The undertaking will reasonably focus:
- (a) on different types of business relationships and VC segments for different sustainability matters;
 - (b) on areas of heightened risk of adverse impacts, affected stakeholder engagement and prioritisation based on criteria of severity and likelihood.
104. For risks and opportunities, this should include how the process considered any other factors in the VC that are sources of IROs, including dependencies from natural and social resources.

IRO-1 - MA methods and assumptions

105. ESRS 2 IRO-1 requires information on methods and assumptions applied in the materiality assessment (ESRS 2 paragraph 53(a)), including thresholds to determine materiality (paragraph 53 b (iv)). This should account for any specifics related to the VC. As per ESRS 2 BP-1, the undertaking should describe the extent of any limitations on the materiality assessment process with respect to the VC.

SBM-3 - Disclosing the outcome of the MA

106. As a result of the materiality assessment, the undertaking shall disclose the material IROs originating its VC. ESRS 2 SBM-3 paragraph 48 (a) requires disclosing “where in its business model, its own operations and its upstream and downstream value chain these material impacts, risks and opportunities are concentrated”.
107. The preparation of this disclosure may use the evidence of impacts from the due diligence process, such as the concentration of types of impacts by country or operational step.
108. ESRS 2 SBM-3 also requires describing the material impacts identified following the materiality assessment process disclosed under IRO-1: “whether the undertaking is involved with the material impacts through its activities or because of its business relationships, describing the nature of the activities or business relationships concerned” (ESRS 2 paragraph 48 c) iv)).
109. ESRS 2 paragraph 48 (b) requires as well disclosure of: “the current and anticipated effects of its material impacts, risks and opportunities on its business model, value chain, strategy and decision-making, and how it has responded or plans to respond to these effects, including any changes it has made or plans to make to its strategy or business model as part of its actions to address particular material impacts or risks, or to pursue particular material opportunities”.



110. This implies that when strategically important hotspots for VC IROs have been identified, ESRS 2 SBM-3 requires information about discussions of the impacts at the relevant managerial level or governance bodies in charge (Paragraph 48(b)).
111. The disclosures should be consistent with the corresponding information on whether and how the VC was considered in the materiality assessment.
112. The information required by ESRS 2 SBM-3 paragraph 48 (a) and (b) (such as effects on and changes of the VC, business strategy and how it responds or plans to respond to those effects) should enable an understanding of the undertaking's basic ability to influence those IROs, and any potential effects on the undertaking.
113. When providing information required by ESRS SBM-3 on material IROs or PAT, qualitative information may be sufficient (for instance for human rights policies with respect to the VC). However, quantitative information may be required to help users understand impacts, their severity and likelihood and/or track the effectiveness of actions to manage them.

FAQ 5: Should VC information be included for Policies, Actions or Targets (PATs) Disclosure Requirements?

114. Yes, for material IROs (including those in the VC), where the undertaking has PATs, it should disclose this (ESRS 2 paragraphs 64(b), 67(b) and 70(b)). Therefore, where a PAT addresses all or some VC actors that should be disclosed. Examples could include:
 - (a) policies to prevent and control pollution by its VC actors;
 - (b) policies against bribery and corruption for VC actors and training for them;
 - (c) actions and resources related to pollution as well as targets to reduce pollution generated by a supplier (ESRS E2 Pollution AR 13 and 19);
 - (d) clauses regarding the respect of fundamental human rights in contracts with VC actors;
 - (e) audits conducted on high-risk suppliers;
 - (f) selection criteria for new suppliers such as the existence of effective grievance mechanisms or freedom of association; and
 - (g) targets for suppliers on sustainable material use for example X% recycled content or X% less waste.
115. VC information coverage is also important for ESRS E1-1 paragraph 16(b) that requires disclosing the decarbonisation levers identified by the undertaking in setting its targets and defining its actions, including levers in the VC. This type of information is expected to be primarily needed in order to set and manage the targets and implement the actions. Reporting is expected to use data existing for such purposes.
116. As a reminder, the undertaking can comply by disclosing that it has not adopted policies and/or actions with reference to the relevant sustainability matter and provide reasons for this. It may also report a timeframe in which it aims to adopt them (ESRS 2 paragraph 62). The same applies to targets (ESRS 2 paragraph 72).
117. In addition, the undertaking should always consider the need to provide entity-specific information. Please refer to paragraph (b) above.
118. In ESRS 4 *Biodiversity and ecosystems*, there are specific requirements dealing with value chain information: ESRS 4-1 Transition plan and consideration of biodiversity and



ecosystems in strategy and business model; as well as topical specification ESRS 2 IRO-1 *Description of processes to identify and assess material biodiversity and ecosystem-related impacts, risks, dependencies and opportunities* as well as ESRS E4-4 (paragraph 32(c)) *Targets related to biodiversity and ecosystems*. These do not necessarily result in the need to collect VC data from actors in the VC solely for the purpose of reporting. The undertaking is expected to leverage on information that is collected for business purposes, e.g., E4-1 par 13, E4 ESRS 2 IRO 1 par 17(a), E4-4 par 32(c).

FAQ 6: Should VC information be included for Metrics Disclosure Requirements?

119. Mostly not. DRs related to metrics cover only own operations except for entity-specific disclosures where the undertaking determines whether VC information is required (see paragraph 122 below). There are the following few metrics set out in the sector-agnostic ESRS that require disclosures of VC information:

- (a) Disclosure Requirement ESRS E1-6 *Gross Scopes 1, 2, 3 and total GHG emissions*;
- (b) Disclosure Requirement ESRS E1-7 *GHG removals and GHG mitigation projects financed through carbon credits*; and
- (c) Disclosure Requirement ESRS E5-4 *Resource inflows* requires a description of resource inflows where material which may include a description of the IROs in the value chain (ESRS 5 paragraph 30). However, when disclosing the quantification of materials used in the production of the undertaking's products and services, this relates only to own operations (ESRS 5 paragraph 31). The undertaking determines whether additional information on the VC is needed on an entity-specific basis.
- (d) ESRS E5-4 par 30 requires a qualitative description of its resource inflows along the upstream value chain. ESRS E2-5 and ESRS E5-5 refers to materials procured and used within the undertaking. While they do not explicitly refer to value chain information, the impacts that arise from the upstream value chain are indirectly covered by the description of the procured material.

120. Following from paragraph 94, ESRS E4 paragraph 36 also refers to life cycle assessment: "If the undertaking has identified material impacts with regards to land-use change, or impacts on the extent and condition of ecosystems, it may also disclose their land-use based on a Life Cycle Assessment." It is also covered in ESRS E4 AR 31: 'With regard to life cycle assessment for land-use, the undertaking may refer to the "Land use related environmental indicators for Life Cycle Assessment" by the Joint Research Center.'

121. With reference to the social standards, ESRS S2 *Workers in the value chain* and S4 *Consumers and end users* cover the VC by definition. ESRS S3 *Affected communities* address impacts on communities affected directly by the undertaking as well as by the actors in the VC. These standards do not specify any metrics, but the ESRS require the undertaking to consider entity-specific metrics, as explained below.

Affected communities suffer the consequences of the undertaking or its VC's operations. However, they are not necessarily part of the VC. For example, an affected community is part of the VC where it provides the land on which the mining takes place.

122. Beyond the specific provisions on metrics in the sector agnostic ESRS, the undertaking shall provide additional VC information metrics or integrate VC data into their metrics, when according to the outcome of its materiality assessment, this is necessary from an



entity-specific perspective (ESRS 1 paragraph 11 and AR 1 to 5 read with ESRS 1 paragraph 65). In particular, ESRS require the undertaking to consider appropriate entity-specific metrics needed for understanding of the impacts or tracking effectiveness of companies' actions. Possible examples are the following:

- (a) impact data of suppliers should be included in the reported metrics, when the undertaking depends in its upstream VC or supply chain from activities that have a high impact on the environment;
 - (b) the percentage of workers in value chains in high-risk areas being covered by social security schemes; and/or
 - (c) the percentage reduction in health and safety incidents compared to incidents in the prior period or as compared to a base period where the quality of the information can be assured.
123. It is important to note that this is relevant only for those activities of VC actors that are associated with material IROs and not for all VC actors.
124. Sector-specific ESRS will cover the inclusion of VC data in its impact metrics when relevant. In the transition period until the ESRS sector standards are available, the undertaking as part of its entity-specific disclosures shall consider this aspect and take inspiration from the available best reporting practices (see ESRS 1 paragraph 131(b)).

FAQ 7: How to assess and quantify the impacts of the VC resulting from business relationships?

125. As set out in the [MAIG FAQ 10 Should the assessment of IROs rely on quantitative information?](#), quantitative measures of impact are the most objective evidence of the severity of an impact. However, quantitative measures may not always be available, and the undertaking may apply quantitative or qualitative thresholds when conducting the MA depending on the circumstances. Refer to the [MAIG chapter 3.6 Deep dive on impact materiality: Setting thresholds](#).
126. For the materiality assessment and for the inclusion of VC data required by metrics, the undertaking may either obtain information directly from actors in its VC or use estimates or proxies or combine both approaches.
127. Obtaining information directly is the most appropriate approach in certain cases, for instance for major tier 1 suppliers (the direct and substantial contractual relationship is a good basis for organising appropriate flows of data) or for customers of products and services in particular when they are end-users (the undertaking knows the parameters of its products and services). When this is the case, the undertaking may need to ask its suppliers and other relationships for information enabling the quantification of the impacts. The undertaking may use questionnaires, surveys and audits to obtain the information. Its buying power and overall contractual influence may help in this regard.
128. It should be noted that the more severe the impact is, there may be a strong incentive to omit such sensitive information, and this could impact the reliability of the information provided by such supplier. This may be particularly relevant for incidents of child or forced labour in the VC.
129. Apart from this issue, the reliability of information directly obtained from the VC may improve over time since VC actors may not be able to quantify their impacts yet but may be in a position to do so in the future given evolution of sustainability reporting. Therefore, supporting such actors to set up effective systems may be important. It may



also be advisable to engage with them and where relevant, also encourage them to do the same with their value chains.

130. Generally, the effort placed on actors in the VC should be proportionate. E.g. the undertaking does not need to query all direct suppliers and could exclude those that deliver insignificant products or services to the undertaking (e.g. a small bakery that delivers pastries once or twice a year for events the undertaking hosts). This would create disproportionate effort for both the reporting company and for the baker who may need to complete similar requests from a multitude of customers. As mentioned above, undertakings do not have to report on each and all value chain actors.
131. As further explained under [FAQ 9 How can estimates be developed when primary data cannot be collected from VC counterparties?](#), the undertaking shall estimate the impact when it cannot collect the necessary data to the required reliability after reasonable effort. Estimates and proxies may be used in combination with information obtained directly as well if quantification is required. Using estimates, similar to financial reporting, is acceptable if organised under a process designed to comply with the characteristics of quality expected from sustainability information. Estimates and proxies may currently be the only available solution to quantify impacts in certain cases, due to unreasonable efforts required to collect data. Examples include tier 2 or tier N suppliers; tier 1 suppliers when they are excessively high in number; customers when they are not end-users (e.g., when the undertaking delivers products or services that are further transformed before contributing to the delivery of products and services to the end-users).
132. An example where obtaining primary data may not be possible and estimates may be used is a beverage company that advises that its drinks are best served cold, i.e., using refrigeration capacity and it has determined energy use as a material matter. This undertaking would find it impossible to precisely measure its impact with each and every customer. However, from its materiality assessment, it assesses that electricity use is a significant part of its impact in the downstream VC. In this case, estimating its impact would involve considering variables such as volumes sold, average time the inventory will be cooled before consumption and an estimate of the average electricity used to cool its products on a unit basis. This may need to also consider location and related prices. Depending on its assessment of the materiality of electricity use, the undertaking may want to provide a sensitivity analysis of its electricity use depending on reasonably possible changes in the important variables in its calculation. Proxies are often available at sector or product level. In all cases the undertaking shall clearly explain the basis for its estimates and the proxies used as well as any factor affecting their consistency over time.
133. ESRS 2 paragraph 10 requires the undertaking to disclose the metrics that include VC data estimated using indirect sources, including the basis for preparation, the resulting level of accuracy and the planned actions to improve accuracy in the future.

FAQ 8: What is 'reasonable effort' to collect VC data?

134. When inclusion of VC information is necessary, under ESRS 1 paragraph 63 or on entity-specific basis, a reporting entity collects information about its upstream and downstream VC only to the extent that this is compatible with a reasonable effort (ESRS 1 paragraph 69) for use in its sustainability statement. In all other circumstances, it shall estimate the missing information based on "all reasonable and supportable information that is available to the undertaking at the reporting date without undue cost or effort" (ESRS 1 paragraph AR17). This includes estimates, sector-average data



and other proxies. For example, an undertaking could use country and sector statistic-based risk assessment data. If more details are known, such as the specific location of farming and manufacturing processes, more specific data may be available. Also refer to paragraph 132 on the necessity to comply with the quality of characteristics requirement.

135. The undertaking should determine the best available way to prepare meaningful VC information and dedicate proportionate resources once the degree of difficulty has been properly assessed.
136. As explained above, the undertaking should report on material IROs in its own operations and in its upstream and downstream VC. In this context, putting the appropriate processes in place is a matter of management decision, internal organisation and allocation of resources. 'Reasonable effort' and 'undue cost or effort' relate to the processes put in place by the undertaking to collect VC information and to the amount of resources dedicated to these processes. "Reasonable effort" cannot be an excuse for no disclosure. 'Reasonable effort' and 'undue cost and effort' depends on facts and circumstances specific to the undertaking. On the basis of [FAQ 7 above](#), using free and publicly available information may in some cases be considered a reasonable effort. In determining whether an action is beyond 'reasonable effort' and/or beyond 'undue cost and effort', the undertaking shall balance the reporting burden of obtaining direct data and the potential lower quality of the information resulting from not undertaking that action. The estimation procedures adopted by the undertaking when direct data are not used are subject to ESRS 2 paragraph 10.
137. For VC data, a good starting point is a deep understanding of what, where and how the inputs for its products and/or services are sourced upstream and/or its products and services are brought to market downstream.
138. ESRS 1 paragraph 68 indicates that the undertaking's ability to obtain VC information may vary depending on factors such as its contractual arrangements, the level of control it may exercise beyond the consolidation perimeter and its buying power. Therefore, there are cases where obtaining the information may be more challenging. In such cases, the undertaking may use other sources of information. For example, an undertaking may have a major exposure to forced labour, because it is getting significant volumes of agricultural commodities and products from jurisdictions where forced labour in agriculture has been documented by the ILO (the International Labour Organisation) and the FAO (Food and Agriculture Organization of the UN). For materiality assessment it is not necessary for the undertaking to change practices and estimate the number of cases of child or forced labour in its value chain. What is important is that it has enough information to conclude that the impacts are severe (based on scale, severity and irremediability).
139. Similarly, undertakings calculating their full environmental footprint, may use estimates not only because it would be unreasonable to get primary data, but also because such data would not be reliable.
140. In the context of materiality assessment, the focus on the VC and VC information should be on where the undertaking is expected to have severe negative impact (on people and the environment). This means that general impact assessments could be useful for the initial work on collecting VC information. Examples include general information about the undertaking's region or sectors of sourcing. For example, where an undertaking is sourcing its products mostly indirectly from Country A and Country B, it may look at available general information about the minimum wage in those countries when considering its social impacts. In Country A the minimum wage is



generally 100% to 120% of the living wage but in Country B the minimum wage is less than 80% of the living wage. Therefore, the exposure to significant impacts is more likely in Country B, all other aspects being constant.

141. For its own governance as well as for purposes of an audit trail for its assurance provider, it would be good for the undertaking to document its efforts, the outcomes and how the information has been incorporated in its reporting process. (Also refer to [MAIG FAQ 12: Should the materiality assessment be documented/evidenced?](#))

FAQ 9: How can estimates be developed when primary data cannot be collected from VC counterparties?

142. As discussed in paragraph 28 above, primary VC information is not required for all disclosures in the sustainability statement. However, where the undertaking determines that VC information is required and primary data (i.e., directly collected from the actor in the VC) is not available, estimated data can be used.
143. When collecting the necessary information from counterparties in the VC is not possible after reasonable effort, ESRS require that the reporting undertaking estimate the missing information, using internal and external information. Such estimates can be used either for assessing material IROs, or for disclosing metrics in the VC, as outlined in ESRS 1 Chapter 5.2. When assessing material IROs in the VC, a combination of primary (i.e. directly collected from the actor in the VC) and estimated data (using secondary data as input) can be employed.
144. Secondary data include data from indirect sources, sector-average data, sample analyses, market and peer groups data, other proxies, or spend-based data.

Examples of external data sources

- Academic institutions such as the Environmental Performance Index
- Government bodies such as the European Social Progress Index of the European Commission and the US Department of State's Social Progress Index,
- Non-profit organisations such as the World Justice Project, or other NGOs.

145. The text box opposite shows some sources of such data. Some of these require a fee and are provided as examples, but ESRS do not require the use of fee-based external sources. These are examples of external sources that help address environmental, social, human rights, and corruption matters.

146. It is difficult to collect VC information necessary to produce the relevant disclosure about impacts caused by indirect business relationships where the undertaking does not have a direct contractual relationship and has less

leverage. If the undertaking cannot collect the necessary data after making reasonable effort to do so, the undertaking may then need to rely on data from indirect sources, like sector-average data, sample analyses, market and peer groups data, other proxies, etc. For example, for VC workers extracting commodities used as components of the undertaking's products, the undertaking may be able to arrange site audits. However, if those actions to obtain primary data and information are not possible after reasonable effort, the undertaking may rely on sector or country data estimating those impacts (e.g., negative impacts on safety, health; risk of child labour etc.) in the location of the mining activities.

147. Disclosing quantitative measures of indirect impacts does not produce relevant information about the undertaking's impact in all circumstances. Consider a manufacturer of bike parts, who uses steel in its products, and therefore has an issue



with pollution generated by its steel production. It is theoretically possible to estimate the volume of pollution/quantify the environmental footprint as some have done. However, this may not be necessary and would not be relevant information, as it would fail to inform about the undertaking's contribution to mitigate the pollution that derives from its products. The undertaking could instead measure its performance in terms of ESRS E5 metrics on circular economy.

148. When a reporting entity does not have data received directly from VC actors, after making reasonable efforts, it shall estimate the information to be reported using sector data or similar data as a starting point (ESRS 1 paragraph 69). Examples include Scope 3 emissions or living wage data of facilities in very high-risk countries, including beyond the first tier of business relationships.
149. As set out in AR 73 of ESRS S1 Own workforce, the WageIndicator is indicated as a potential source (with others) for calculating adequate wage benchmarks outside of the EEA as the last option in the hierarchy. The WageIndicator provides information about minimum and living wages for more than 200 countries which could be an example of applicable benchmarks as referred to under ESRS S1-10 Adequate wages. Undertakings can use this information to explain prioritisation of actions and targets in specific countries or regions for both own workforce and workers in the VC. The information from such sources could form part of the undertaking's explanation under ESRS 2 SBM-3 of how it identified and assessed material IROs. The exact living wages may differ in certain facilities and are dependent on the composition of the family of a worker, however these sources can be useful in the context of the materiality assessment. Once wage has been identified as a material risk, it can be that more accurate data is needed to set targets and to report on progress.
150. Undertakings need to be aware that setting up a reliable data collection system which includes VC partners takes time. They may consider processes and controls to collect data and report the information. The quantity and quality of VC information is likely to improve over time, but until then sector data or similar sources can be a good starting point. As mentioned in paragraph 28 above, information about each and every actor in the VC is not required.
151. The use of appropriate estimates or proxies is critical for the quality of reported information. The origin of the data may influence the quality of the information provided in the sustainability statement. Therefore, transparent disclosure and explanation of the use of estimates are essential.
152. ESRS 2 BP-2 paragraph 10 requires preparers to:
 - (a) identify the metrics for which estimates are used;
 - (b) describe the basis for preparation,
 - (c) the resulting level of accuracy and,
 - (d) where applicable, the planned actions to improve the accuracy in the future.

FAQ 10: Is a case of bribery not involving an employee relevant for the reporting entity?

153. Consider a case where Q, an employee at a customer (XYZ) of the reporting undertaking (ABC), was found to have been bribed by S, an employee at one of XYZ's suppliers. In this case, ABC would not have to disclose this under the metrics of ESRS G1-4, as an employee of the reporting undertaking is not involved in the case and as



explained in ESRS G1 paragraph 26. However, ABC would consider this information when it considers the risks around corruption and bribery in the sector/geographical area going forward.

4. VC map

154. The table below maps the disclosure requirements in the sector-agnostic ESRS and whether reporting undertakings have to report VC information.

155. The VC map below does not cover disclosures that fall under entity-specific disclosures mandated under ESRS 1 paragraph 11. It is the responsibility of the undertaking to determine whether entity-specific VC information is required to allow users to understand the undertaking's material IRO's and/or to meet the qualitative characteristics of information per Appendix B of ESRS 1. (Paragraph 65 of ESRS 1)

VC coverage map of Set 1 ESRS

Level of VC coverage		Disclosure Requirements with this level of VC coverage			
1. The undertaking shall assess its material IROs across its VC		IRO-1			
2. The undertaking shall describe its VC		SBM-1 ^a			
3. The undertaking shall describe its material IROs and report where in the VC they arise		SBM-3 ^a			
4. The undertaking shall reflect whether and how policies, actions or targets (PAT) cover VC.	BP-1/2 ^a , SBM-2, GOV-4/5	E1-2 to E1-4 E2-1 to E2-3, E3-1 to E3-3,	E4-1 to E4-4, E5-1 to E5-3, S1-1 to S1-5	S2-1 to S2-5 S3-1 to S3-5 S4-1 to S4-5	G1-1, G1-2, G1-3
5. The standard covers PAT for IROs that are linked to people in the VC . The undertaking shall disclose whether and how PAT cover VC.		S2 S3 ⁴ S4			
6. The disclosure only reflects own operations , as no coverage of VC is required	GOV-1/3, IRO-2, E1-5	E1-8 -E1-9, E2-4 ^a , E2-6,	E3-4/5 E4-5/6 E5-4 par 31	S1-1 to S1-17 ⁵	G1-4 to G1-6
7. Disclosure of procured materials		E2-5 ^a E5-5 ^a			
8. There are specific quantitative datapoints in this DR that requires VC coverage ⁶		E1-6 E1-7			
9. There are specific qualitative datapoints in this DR that requires VC coverage ⁷		E1-1 E4-1 par 13		E4 IRO 1 par 17(a) E4-4 par 32(c) E5-4 par 30	
10. SFDR indicators ⁸ listed in ESRS 2 Appendix B	VC to be covered to the extent that foreseen in the relevant technical standards				
11. Other EU law (excluding SFDR) in ESRS 2 Appendix B		VC to be covered			

⁴ The standard ESRS S3 *Affected communities* covers a group of people that may also part of the undertaking's upstream and downstream VC when they also have business relationships with the undertaking.

⁵ Some consider DR S1-7 as requiring information about the VC however, these employees form part of own workforce and therefore own operations.

⁶ Coverage of VC information does not mean necessarily collection of data from actors in the value chain, see paragraphs 125 to 126 above.

⁷ Coverage of VC information does not mean necessarily collection of data from actors in the value chain, see paragraphs 125 to 126 above.

⁸ The SFDR regulation is open for consultation and changes may follow.



156. The above table should be read with the following additional notes for those DRs marked with the symbol [¶].

DR	Content
BP-1	To what extent the sustainability statement covers the undertaking's upstream and downstream VC.
BP-2	When metrics include VC data estimated using indirect sources, such as sector-average data or other proxies, the undertaking shall: <ol style="list-style-type: none"> i. identify the metrics; and ii. describe the basis for preparation, E4-1 par 13 iii. the resulting level of accuracy and, iv. where applicable, the planned actions to improve the accuracy in the future.
SBM-1	Requires that value chain is covered but is not expected to trigger data requests to actors in the value chain, i.e. can be covered by internal or public information.
SBM-3	For each material IRO identified in the materiality assessment, the undertaking shall report whether the undertaking is involved with the negative or positive impact through its activities or because of its business relationships.
E2-4	AR 20 refers to procurement of microplastics
E2-5	Relates to the products/materials and/or substances procured which ends up in products / manufacturing.
E5-5	Includes supplied material but does not expand to suppliers
E5-6	Waste treatment may sometimes require information from supplier who treats waste

157. Per paragraph 114, for material IROs where the undertaking has policies, actions and targets covering the VC, it should disclose this (ESRS 2 paragraphs 64(b), 67(b) and 70(b)). If not, either because the undertaking does not have such a PAT or because it does not cover the VC, the undertaking will comply by indicating this.

158. The names of the disclosure requirements are provided in Appendix A.



Appendix A: Names of disclosure requirements

1. The list of names of the disclosure requirements is to help in the use of the VC map.

ESRS 2 - General disclosures
DR 2-BP-1 - General basis for preparation of sustainability statement
DR 2-BP-2 - Disclosures in relation to specific circumstances
DR 2-GOV-1 - The role of the administrative, management and supervisory bodies
DR 2-GOV-2 - Information provided to and sustainability matters addressed by the undertaking's administrative, management and supervisory bodies
DR 2-GOV-3 - Integration of sustainability-related performance in incentive schemes
DR 2-GOV-4 - Statement on due diligence
DR 2-GOV-5 - Risk management and internal controls over sustainability reporting
DR 2-SBM-1 - Strategy, business model and value chain
DR 2-SBM-2 - Interests and views of stakeholders
DR 2-SBM-3 - Material IROs and their interaction with strategy and business model
DR 2-IRO-1 - Description of the processes to identify and assess material IROs
DR 2-IRO-2 - Disclosure Requirements in ESRS covered by the undertaking's sustainability statement
Policies MDR-P - Policies adopted to manage material sustainability matters
Actions MDR-A - Actions and resources in relation to material sustainability matters
Metrics MDR-M - Metrics in relation to sustainability matters
Targets MDR-T - Tracking effectiveness of policies and actions through targets
ESRS E1 - Climate change
DR E1-1 - Transition plan for climate change mitigation
DR E1-2 - Policies related to change mitigation and adaptation
DR E1-3 - Actions and resources in relation to climate change policies
DR E1-4 - Targets related to climate change mitigation and adaptation
DR E1-5 - Energy consumption and mix
DR E1-6 - Gross Scopes 1, 2, 3 and Total GHG emissions
DR E1-7 - GHG removals and GHG mitigation projects financed through carbon credits
DR E1-8 - Internal carbon pricing
DR E1-9 - Anticipated financial effects from material physical and transition risks and potential climate-related opportunities
ESRS E2 - Pollution
DR E2-1 - Policies related to pollution
DR E2-2 - Actions and resources related to pollution
DR E2-3 - Targets related to pollution
DR E2-4 - Pollution of air, water and soil
DR E2-5 - Substances of concern and substances of very high concern
DR E2-5 - Anticipated financial effects from pollution-related IROs
ESRS E3 - Water and marine resources
DR E3-1 - Policies related to water and marine resources
DR E3-2 - Actions and resources related to water and marine resources
DR E3-3 - Targets related to water and marine resources
DR E3-4 - Water consumption
DR E3-5 - Anticipated financial effects from water and marine resources-related IROs
ESRS E4 - Biodiversity and ecosystems
DR E4-1 - Transition plan and consideration of biodiversity and ecosystems in strategy and business model
DR E4-2 - Policies related to biodiversity and ecosystems
DR E4-3 - Actions and resources related to biodiversity and ecosystems
DR E4-4 - Targets related to biodiversity and ecosystems
DR E4-5 - Impact metrics related to biodiversity and ecosystems change
DR E4-6 - Anticipated financial effects from biodiversity and ecosystem-related IROs
ESRS E5 - Resource use and circular economy
DR E5-1 - Policies related to resource use and circular economy
DR E5-2 - Actions and resources related to resource use and circular economy
DR E5-3 - Targets related to resource use and circular economy



ESRS E5 - Resource use and circular economy
DR E5-4 - Resource inflows
DR E5-5 - Resource outflows
DR E5-6 - Anticipated financial effects from material resource use and circular economy-related IROs
ESRS S1 - Own workforce
DR S1-1 - Policies related to own workforce
DR S1-2 - Processes for engaging with own workforce and workers' representatives about impacts
DR S1-3 - Processes to remediate negative impacts and channels for own workforce to raise concerns
DR S1-4 - Taking action on material impacts on own workforce, and approaches to mitigating material risks and pursuing material opportunities related to own workforce, and effectiveness of those actions
DR S1-5 - Targets related to managing material negative impacts, advancing positive impacts, and managing material risks and opportunities
DR S1-6 - Characteristics of the undertaking's employees
DR S1-7 - Characteristics of non-employee workers in the undertaking's own workforce
DR S1-8 - Collective bargaining coverage and social dialogue
DR S1-9 - Diversity metrics
DR S1-10 - Adequate wages
DR S1-11 - Social protection
DR S1-12 - Persons with disabilities
DR S1-13 - Training and skills development metrics
DR S1-14 - Health and safety metrics
DR S1-15 - Work-life balance metrics
DR S1-16 - Compensation metrics (pay gap and total compensation)
DR S1-17 - Incidents, complaints and severe human rights impacts
ESRS S2 - Workers in the value chain
DR S2-1 - Policies related to value chain workers
DR S2-2 - Processes for engaging with value chain workers about impacts
DR S2-3 - Processes to remediate negative impacts and channels for value chain workers to raise concerns
DR S2-4 - Taking action on material impacts on value chain workers, and approaches to managing material risks and pursuing material opportunities related to value chain workers, and effectiveness of those actions
DR S2-5 - Targets related to managing material negative impacts, advancing positive impacts, and managing material risks and opportunities
ESRS S3 - Affected communities
DR S3-1 - Policies related to affected communities
DR S3-2 - Processes for engaging with affected communities about impacts
DR S3-3 - Processes to remediate negative impacts and channels for affected communities to raise concerns
DR S3-4 - Taking action on material impacts on affected communities, and approaches to managing material risks and pursuing material opportunities related to affected communities, and effectiveness of those actions
DR S3-5 - Targets related to managing material negative impacts, advancing positive impacts, and managing material risks and opportunities
ESRS S4 - Consumers and end-users
DR S4-1 - Policies related to consumers and end-users
DR S4-2 - Processes for engaging with consumers and end-users about impacts
DR S4-3 - Processes to remediate negative impacts and channels for consumers and end-users to raise concerns
DR S4-4 - Taking action on material impacts on consumers and end-users and approaches to managing material risks and pursuing material opportunities related to consumers and end-users, and effectiveness of those actions
DR S4-5 - Targets related to managing material negative impacts, advancing positive impacts, and managing material risks and opportunities
ESRS G1 - Business conduct
DR G1-1 - Business conduct policies and corporate culture
DR G1-2 - Management of relationships with suppliers
DR G1-3 - Procedures to address corruption or bribery
DR G1-4 - Incidents of corruption or bribery
DR G1-5 - Political influence and lobbying activities
DR G1-6 - Payment practices

